Deutsches Aktieninstitut

Retail Financial Services

Deutsches Aktieninstitut's response to the
EU Commission's Green Paper

Position Paper of Deutsches Aktieninstitut [Transparency Reg. 38064081304-25]
regarding the EU Commission's Green Paper on Retail Financial Services
(COM(2015) 630 final on 10th of December 2015), March 17th 2016.

Summary

On 10th of December 2015 the EU Commission has published its Green Paper on retail financial services - Better products, more choice, and greater opportunities for consumers and businesses (COM(2015) 630 final). The Green Paper provides a basis for discussing, how to improve

- the EU-wide offer of retail financial services and
- the EU-wide access to retail financial services.

In this context, the consultation shall determine, how the market for retail financial services can be further opened up, whilst maintaining an adequate level of consumer and investor protection.

Deutsches Aktieninstitut appreciates the initiative of the EU Commission. However, the baseline assumptions of the Green Paper do not properly reflect the present situation and consequently could lead to a legislative outcome, which brings rather distortions to the market than improvements.

Scope of the Initiative

The wide scope of the Green Paper, including “all” retail financial services - namely insurance, loans, payments, current and savings accounts and other retail investments -, could lead to unintended negative consequences on some of these products.

Many of the problems mentioned in the Green Paper are for example not valid for capital market products.Therefore, we worry that regulation intended to promote the other services within the scope of the Green Paper will adversely affect retail investments at the end, e.g. through higher regulatory burdens or costs.

Proper Assessment to unambiguously identify Market Demand

Discussing the necessity to increase the offer of financial services across borders, the demand or interest of retail customers in buying such products abroad should be analyzed at first. Only if they are interested in buying products all across the EU, financial institutions will develop a business case to actually offer them these services. Therefore, the EU Commission needs to distinguish between a situation, in which consumers are actually not interested in such everywhere accessible products because they may have enough options in their own country or do not want to rely on foreign financial providers, and a situation, in which they would like to buy such products but cannot due to a supply shortage.

Careful Assessment of New Initiatives and Legislation

For products for which a demand across the EU could be assumed an important issue are distinct and sometimes even contradictory national regulation and conditions in different Member States. Companies have to consider a multitude of different regulations, e.g. civil rights, taxation rules, money laundering, contract law, liability, consumer protection or bankruptcy law, which strongly differ across Member States. In order to be able to offer retail financial services everywhere, the EU Commission would need to establish a stable and common cross-border regulatory framework.

The timing of new proposals is also important. The quality of legislation suffers under the constant adoption of subsequent regulation, just after new rules have been put into force or even before. Thus the legislator is not able to take into account the impact of the preceding regulation while already adopting the next one. Therefore, before deliberating proposals for new regulatory measures, the EU Commission should pursue their own better regulation approach. The proposals should be subject to a comprehensive impact assessment and only be pursued further, if a positive welfare effect will be generated.

Digitalisation

Digitalization has the potential to facilitate an EU-wide offer of certain financial services and a better access for retail customers to these servcies. Yet, the focus of the EU Commission should not only lie on the FinTech sector but on digitalization in the financial sector in general. New as well as traditionel companies face similar problems and opportunities and thus should be treated equally.

Questions

Question 1A: For which financial products could improved cross order supply increase competition on national markets in terms of better choice and price?

No answer.

Question 2A: What are the barriers which prevent firms from directly providing financial services cross-border?

Deutsches Aktieninstitut considers the following barriers as the most relevant ones (among the choices given):

- Differences in national legislation
- Additional requirements imposed by national regulators
- Impossibility of verifying the identity of cross-border customers
- Cost of servicing clients cross-border (without local infrastructure)

Other barriers, which prevent firms from directly providing financial services cross-border are:

- Distinct and sometimes even contradictory national regulation and conditions in different Member States.
- Risk assessment or credit analysis of customers across borders is impossible or highly complex. National documentation differs in structure and language. Moreover, financial institutions have to consider a range of national particularities, which they have no knowledge of.
- Different pre-contractual information and advisory duties across Member States and on EU level.

Question 3: Can any of these barriers be overcome in the future by digitalisation and innovation in the FinTech sector?

Deutsches Aktieninstitut believes that the following barriers can be overcome by digitalisation (among the choices given):

- Impossibility of verifying the identity of potential cross-border clients
- Lack of knowledge of other markets
- Lack of knowledge of the offer of products in another Member State
- Lack of knowledge of redress procedures in another Member State
- Cost of servicing clients cross-border (without local infrastructure)
- Other

It should be noted in advance that the focus of the EU Commission should not only lie on the FinTech sector but on digitalization in the financial sector in general, as traditional financial institutions also invest in digitizing and innovating financial services. By now, both groups mostly cooperate with each other.

Moreover, a large part of the problem seems to be on the demand side. Thus it is likely that FinTechs face the same or similar problems as traditional financial institutions. We will see, if digitalization will help to overcome these problems. Yet, this will concern FinTechs and financial institutions equally. Therefore, it is important that financial institutions and FinTechs face the same rules and regulatory requirements, in order to ensure a level playing field and same levels of protection.

In general, digitalization enables companies to offer products without needing local infrastructure. This could save costs and reduce barriers. However, often barriers, preventing an EU wide offer, do not arise from a lack of innovation and digitalization in financial institutions but from distinct national legislations or an insufficient regulatory framework for cross national product offers. For example no EU wide accepted procedure for customer identification to open a bank account across borders has yet been established.

On the other hand, generation and usage of big data presents a real opportunity. New digitized tools will generate large amounts of data, which then can be used by companies to offer individualized products actually meeting customer expectations. This in turn could improve the customer experience considerably.

Evaluating the possible advantage of digitalization and innovation on the financial sector, it should be differentiated between standardized products and products requiring extensive advisory services. The distribution of standardized, simple products is likely to be facilitated by using new digitized tools. An example are so-called robo advisors, automated investment brokerage by a software, which provide easy access to capital market products like funds or ETFs. However, products requiring extensive advisory services or products for which financial institutions need detailed information to evaluate the credibility of customers will hardly benefit of the new tools.

Likewise, the costs of servicing clients for such sophisticated products cross-border without local infrastructure can hardly be reduced through digitalization and innovation. The advantage of cost reductions and a larger customer base through the internet contrary to “physical” distribution depends on the possibility to offer the same standardized product to customers in all countries. If different regulations have to be considered and thus adapted products need to be developed for each country, the costs-benefit analysis for financial institutions will be rather negative. The EU passport, which allows firms authorised in one Member State to provide its services in another Member State with reduced administrative burdens and a minimum of paperwork, cannot solve this problem entirely. Companies, authorized by supervision in one Member State, are allowed to offer their products everywhere within the EU, protecting them from disctinct national supervisory regimes. Moreover, international private law permits companies to decide, which national regime they apply to their “cross-border” products. Yet, they still could be charged for violation of national civil law, if following their own national civil legislation and not the local one. Thus providers will be reluctant to offer products EU wide. However, this in turn does not mean that they should be officially obliged to offer their products across borders. This decision should still be left to their own evaluation and decision.

Question 4: What can be done to ensure that digitalisation of financial services does not result in increased financial exclusion, in particular of those digitally illiterate?

No answer.

Question 5: What should be our approach if the opportunities presented by the growth and spread of digital technologies give rise to new consumer protection risks?

No answer.

Question 6: Do customers have access to safe, simple and understandable financial products throughout the European Union?

The wide scope of the Green Paper, including "all" retail financial services - namely insurance, loans, payments, current and savings accounts and other retail investments -, could lead to unintended negative consequences on some of these products. While other retail investments also comprehend investments in capital market products, the main focus of the Green Paper clearly lies on the other financial services, like insurances and banking products.

Many of the problems mentioned in the Green Paper are not valid for capital market products, as it is quite easy to buy securities or funds from different nations. However, Deutsches Aktieninstitut worries that regulation intended to promote the other products within the scope of the Green Paper, will adversely affect retail investments at the end, e.g. through higher regulatory burdens or costs. A present example for such unintended side effects – under the slogan consumer protection - is the increasing regulation of investment advice. The biggest changes were probably triggered by the financial market directive MiFID. The most recent revision of this directive further intensified the investment advice legislation. Among others, the German "Beratungsprotokoll" (investment advice minutes) has been introduced on European level.

Experience with the German "Beratungsprotokoll" shows that the formalized procedure to record investment advice is very time-consuming. In addition, due to the documentation requirements banks have to devote a huge amount of resources to implement the respective processes. As unintended side effect, many (especially smaller) banks abandoned its investment advice in shares completely and others reduced their investment advice in shares significantly. A survey conducted by Deutsches Aktieninstitut among German banks in July 2014 provides evidence. Regulation is also a main reason why banks retreat from investment advice in other securities like bonds and investment funds.

Moreover, customers complain about the additional time consumed and would prefer to waive this obligation individually – unfortunately, they are not allowed to do so. The development that banks refrain from share recommendations will further harm equity culture among retail investors. Thus the legislator should re-evaluate the benefits of investment advice minutes in particular and the regulation of investment advice in general.

Another issue is that the EU Commission may overestimate the knowledge of consumers about financial services and processes. Many people have problems understanding domestic products. So, why should they buy foreign products, which are "even more complicated"? Or maybe they do not want to? In that case no regulatory effort can solve this problem. It would be important to define the real needs and reasons of retail investors first, before tackling the regulatory framework. Depending on the outcome of such an anlysis, other measures like upgrading digital infrastructure, offering financial planning support or other "soft issues" could create an additional impact.

For the benefit of ensuring effective retail customer protection we should rather create an environment providing for widespread financial and economic literacy than pursuing an ecosystem with even more regulatory requirements for financial institutions. Retail customers must be enabled to make sound investment decisions in their own responsibility. They should be put in a position to evaluate and compare financial products and to make informed and sensible investment decisions. Future efforts to reform the European framework for retail financial servcies thus should focus on a widespread economic literacy as core element.

Question 7: Is the quality of enforcement of EU retail financial services legislation across the EU a problem for consumer trust and market integration?

From the point of view of Deutsches Aktieninstitut inconsistencies in legislation and timing of new proposals constitute a barrier for integrated and well-functioning financial markets across the EU.[1]

One issue regarding retail financial services legislation are differences across Member States. The implementation and application of EU regulation factually differ considerably. Furthermore, the time of implementation in effect can also vary. Although every new Directive or rule has an official implementation date, it might be implemented timely in some Member States but not in other ones. In such situations retail customers and financial institutions equally face unknown and varying conditions and thus risks across borders.

Furthermore, before deliberating proposals for new regulatory measures, the EU Commission should pursue their own better regulation approach. The proposals should be subject to a comprehensive impact assessment and only be pursued further, if a positive welfare effect will be generated.

Another issue is the timing of new proposals. The quality of legislation suffers under the constant adoption of subsequent regulation, just after new rules have been put into force or even before. Thus the legislator is not able to take into

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[1] Compare among others the position of Deutsches Aktieninstitut on the Green Paper on building a Capital Markets Union on 12.05.2015 https://www.dai.de/de/das-bieten-wir/positionen/positionspapiere.html?d=337 or on the Call for Evidence: EU regulatory framework for financial services on 21.09.2016 https://www.dai.de/de/das-bieten-wir/positionen/positionspapiere.html?d=369.

account the impact of the preceding regulation while already adopting the next one. It should therefore be considered to first await the forthcoming adoption of the new Data Protection Directive or the NIS Directive as well as the national implementation of present legislation packages like MCD, PSD II, PAD and MiFID II. And afterwards evaluate their effects before any ideas for new proposals are brought up.

In contrast, the EU passport (allowing firms authorised in one Member State to provide its services in another Member State with reduced administrative burdens and a minimum of paperwork) and the ARD Directive (same terms for all out-of-court redress bodies wihtin the EU) should help to foster market confidence. They are steps in the right direction. However, they will not solve all the barriers described above.

Question 8: Is there other evidence to be considered or are there other developments that need to be taken into account in relation to cross-border competition and choice in retail financial services?

Discussing the necessity to increase the offer of financial services across borders, the demand or interest of retail customers in buying such products abroad should be analyzed at first. Only if they are interested in buying products all across the EU, financial institutions will develop a business case to actually offer them these services. Therefore, the EU Commission needs to distinguish between a situation, in which consumers are actually not interested in such everywhere accessible products because they may have enough options in their own country or do not want to rely on foreign financial providers, and a situation, in which they would like to buy such products but cannot due to a supply shortage.

Referring thereto, consumers currently seem to have a sufficient range of products and alternatives to choose from in larger countries like Germany. Further underpinning the impression that they are maybe not interested in purchasing foreign products. This is also supported by the fact that smaller countries like Luxembourg have a much higher rate of cross-border purchases than larger ones. The same is true for border areas, where people are used to purchase services or products on either side, taking advantage of price and service level difference.

Another issue is that the digitalization of financial services increases the influence and importance of big technology corporations on this market. These corporations basically own the interface between consumers and service providers, e.g. as producers of mobile devices or software, and thus can easily manipulate the access to certain financial services. In this context, it has to be ensured that big technology corporations cannot influence market demand by privileging own tools and services, while simultaneously discriminating offers of competitors.

Question 9: What would be the most appropriate channel to raise consumer awareness about the
different retail financial services and insurance products available throughout the Union?

No answer.

Question 10: What more can be done to facilitate cross-border distribution of financial products through intermediaries?

No answer.

Question 11: Is further action necessary to encourage comparability and / or facilitate switching to retail financial services from providers located either in the same or another Member State?

No answer.

Question 12: What more can be done at the EU level to tackle the problem of excessive fees charged for cross-border payments (e.g. credit transfers) involving different currencies in the EU?

No answer.

Question 13: In addition to already existing disclosure requirements*, are there any further actionsneeded to ensure that consumers know what currency conversion fees they are being charged when they make cross-border transactions?

No answer.

Question 14: What can be done to limit unjustified discrimination on the grounds of residence in the retail financial sector including insurance?

No answer.

Question 15: What can be done at the EU level to facilitate the portability of retail financial products – for example, life insurance and private health insurance?

No answer.

Question 16: What can be done at the EU level to facilitate access for service providers to mandatory professional indemnity insurance and its cross-border recognition?

No answer.

Question 17: Is further action at the EU level needed to improve the transparency and comparability of financial products (particularly by means of digital solutions) to strengthen consumer trust?

Deutsches Aktieninstituts takes the view that no more action is required to strengthen consumer trust. There are already numerous measures to increase transparency on products in the existing regulation (CCD, PAD, MiFID, PRIIPs or IDD). Not all Member States have already implemented these directives, their impact can not yet be assessed. New measures should therefore not yet be undertaken. The regular review procedures of the current framework should be used to make sure that information is provided as consistently, easy and comprehensible as possible.

Question 18: Should any measures be taken to increase consumer awareness of FIN-NET* and its effectiveness in the context of the Alternative Dispute Resolution Directive's implementation?

No answer.

Question 19: Do consumers have adequate access to financial compensation in the case of mis-selling of retail financial products and insurance?

No answer.

Question 20: Is action needed to ensure that victims of car accidents are covered by guarantee funds from other Member States in case the insurance company becomes insolvent?

No answer.

Question 21: What further measures could be taken to enhance transparency about ancillary insurance products and to ensure that consumers can make well-informed decisions to purchase these products?

No answer.

Question 22: What can be done at the EU level to support firms in creating and providing innovative financial digital services across Europe, with appropriate levels of security and consumer protection?

It is not that simple to offer retail financial services across borders. Although digitalisation opens up the possibility to provide several products to customers without local infrastructure, it cannot solve the issue of legislative differences and uncertainties regarding risks and particularities in national markets.

Companies have to consider a multitude of different regulations, e.g. civil rights, taxation rules, money laundering, contract law, liability, consumer protection or bankruptcy law, which strongly differ across Member States. The same can be said about retail customers, who are reluctant to purchase products under little known conditions. In order to be able to offer retail financial services everywhere, the EU Commission would need to establish a stable and common cross-border regulatory framework.

Only then financial institutions will be willing to offer such products across the EU and consumers will be ready to buy them. Yet, as explained before, this only concerns products for which an actual cross-border demand exists (compare question 8). Moreover, the EU Commission should evaluate every planned regulatory change beforehand and determine, if it brings facilitation and creates an actual benefit or just increases the regulatory burder and costs (compare questions 6 and 7).

Question 23: Is further action needed to improve the application of European Anti-Money Laundering legislation, particularly to ensure that service providers can identify customers at a distance, whilst maintaining the standards of the current framework?

No answer.

Question 24: Is further action necessary to promote the uptake and use of e-ID and e-signatures in retail financial services, including as regards security standards?

No answer.

Question 25: In your opinion, what kind of data is necessary for credit-worthiness assessments?

No answer.

Question 26: Does the increased use of personal financial and non-financial data by firms (including traditionally non-financial firms) require further action to facilitate provision of services or ensure consumer protection?

No answer.

Question 27: Should requirements about the form, content or accessibility of insurance claims histories be strengthened (for instance in relation to period covered or content) to ensure that firms are able to provide services cross-border?

No answer.

Question 28: Is further action necessary to support firms in providing post-contractual services in another Member State without a subsidiary or branch office?

No answer.

Question 29: Is further action necessary to encourage lenders to provide mortgage or loans cross-border?

No answer.

Question 30: Is action necessary at the EU level to make practical assistance available from Member State governments or national competent authorities (e.g. through 'one-stop-shops') in order to facilitate cross-border sales of financial services, particularly for innovative firms or products?

No answer.

Question 31: What steps would be most helpful to make it easy for businesses to take advantage of the freedom of establishment or the freedom of provision of services for innovative products (such as streamlined cooperation between home and host supervisors)?

No answer.

Question 32: For which retail financial services products might standardisation or opt-in regimes be most effective in overcoming differences in the legislation of Member States?

No answer.

Question 33: Is further action necessary at the EU level in relation to the 'location of risk' principle in insurance legislation and to clarify rules on 'general good' in the insurance sector?

No answer.

Question 34: Please provide any additional comments in the box below:

No answer.

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